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In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 209

UNITED STATES OF AMERICA, PETITIONER

v.

JOHN WATERHOUSE, ERNEST HAY WODEHOUSE, WALTER FRANCIS FREAR AND JOHN EDWARD RUSSELL, TRUSTEES UNDER THE WILL AND OF THE ESTATE OF SAMUEL M. DAMON, DECEASED

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The district court did not write an opinion. The opinion of the circuit court of appeals (R. 457–464) is reported in 132 F. 2d 699.

JURISDICTION

The judgment of the circuit court of appeals was entered January 6, 1943 (R. 464). A petition for rehearing was denied March 2, 1943 (R. 464). The petition for a writ of certiorari was filed July

29, 1943, within the time as extended by a Justice of this Court (R. 465) and was granted October 11, 1943 (R. 471). The jurisdiction of this Court rests upon section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether, in determining the value of agriculture land claimed to be adaptable for subdivision purposes, the jury may consider testimony that the present value of the land is a figure arrived at by capitalizing the income which, in the opinion of the witnesses, would be produced if the lands were subdivided and leased for dwellings, business places, and truck gardens.

2. Whether just compensation for lands condemned includes the increment the owner might realize by withholding from sale other competitive lands.

3. Whether just compensation includes increases in the value of lands condemned, resulting from authorization of the project for which they are taken.

STATEMENT

In 1939 the United States began to expand its military installations at Pearl Harbor Navy Yard and Hickam Field. Between April 26, 1939 and September 9, 1940, Congress appropriated some $30,000,000.00 for specific projects at this naval and military base.[1] During this same period

[1] See Act of April 26, 1939, 53 Stat. 592, 607; Act of May 25, 1939, 53 Stat. 757; Act of August 9, 1939, 53 Stat. 1301,

consideration was given to the housing requirements of Army and Navy personnel and national defense workers, particular attention being given to the problems in Hawaii.[2] For the purpose of providing such housing in Hawaii the Act of May 25, 1939, 53 Stat. 757, 774, included an appropriation of $165,000.00 for acquisition of the necessary site. The hearings on this item show that the tract to be acquired was approximately 350 acres of sugar-cane lands, contiguous to Pearl Harbor and Hickam Field, owned by the Damon Estate. See Hearings on Navy Department Appropriation Bill for 1940, H. Subcommittee on Appropriations, 76th Cong., 1st sess. (1939), p. 416; Appendix, *infra* pp. 37–39.

Accordingly, in November 1940, the United States instituted two condemnation proceedings, accompanied by declarations of taking, to acquire this land, one suit (No. 436 in the district court) embracing 254.468 acres for the Navy Department (R. 42, 51) and the other (No. 434 in the district court) 77.288 acres for army housing

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1322; Act of June 11, 1940, 54 Stat. 265, 281, 294; Act of June 13, 1940, 54 Stat. 350, 361; Act of September 9, 1940, 54 Stat. 872, 877, 880.

[2] Act of May 25, 1939, 53 Stat. 757, 774; Act of June 2, 1939, 53 Stat. 798; Act of June 28, 1940, 54 Stat. 676, 681; Act of September 9, 1940, 54 Stat. 872, 883; Lanham Act of October 14, 1940, 54 Stat. 1125; see 84 Cong. Rec. pt. 6, p. 5808 (1939); S. Rep. 390, 76th Cong., 1st sess. (1939); H. Rep. 192, 76th Cong., 1st sess. (1939); H. Rep. 2706, 76th Cong., 3d sess. (1940).

(R. 11, 19). The Government deposited estimated compensation totalling $157,369.94 for the land and improvements (R. 17, 59).[3] Inasmuch as the lands involved in the two suits are contiguous and both owned by the Damon Estate, the proceedings were consolidated for trial (R. 103). The cases were tried before a jury which returned verdicts totalling $265,404.80 (R. 440–441). The disputed questions here raised relate to the method by which respondents were permitted to prove value. The valuation evidence may be summarized as follows:

With the exception of a two-acre parking lot (R. 322–325), all of the lands condemned were, at the time of taking, used for growing sugar cane (R. 158). The owners, the trustees of the Damon Estate, had leased a total of 1,451.66 acres, including the 331 acres here involved, to the Honolulu Plantation Company for a term of 15 years from January 1, 1929, at an average annual rental of $23.50 an acre for the sugar-cane lands (R. 312–313). Experts for the Government stated that the best use of most of the lands was for the growing of sugar cane but that certain highway frontage had some additional value because of the possibility of use for residential or business purposes. These witnesses valued the lands at a total of

[3] Of the amount deposited, $15,639.90 was allocated to growing crops and improvements claimed by the lessee, the Honolulu Plantation Company (R. 59). The value of these items is not here involved (R. 103).

$137,487.00, based upon a selling price per square foot. (R. 117–125, 134–140.)

Respondents took the view that all of the lands had outgrown the category of cane lands and were best suited for subdivisions into residence lots and truck farms (R. 154–155). Based upon this theory, respondents' four experts reached values ranging from $309,279.78 to $514,345.17 (R. 160, 167, 169, 206, 209, 240, 243, 246–247, 321, 325, 330). Castro, the first witness, assumed subdivision of the land into lots which could be leased for dwellings, business places, and truck gardens. He then determined the average yearly "net" rent[4] which he estimated could be obtained from such a subdivision and capitalized such rentals at four percent. The result he called fair market value at the date of taking. (R. 160–161, 167, 169.) Respondents' next two witnesses, Harrison and Kearns, who collaborated on their appraisals (R. 260), followed a similar method of determining "fair market value." They divided each parcel into two types of land, residence property near the highways and truck farm lots to the rear. They capitalized at five percent an estimated rental on the truck farm lots, and they put a selling price upon each residence lot. (R. 210–213, 240–242, 262). The last witness as to value was

[4] This "net" rental assumed that the lessee would pay all taxes, improvement assessments, water rates, and similar charges (R. 194).

respondent Russell, who was chosen to represent the other trustees (R. 340). He envisaged subdivision of the entire area into lots which could be leased for residence and business purposes. He capitalized at four percent the estimated income from such leases after deduction of expenses. (R. 314, 319, 321, 325–326.)

All of these opinions were based upon the belief that a demand for residence and truck farms existed and would continue in the future (R. 169, 181–182, 205, 206, 207, 227, 239, 242–243, 248–249, 285–287, 317, 320, 345–346, 353). To support this view Russell and Sam Damon, a beneficiary of the Damon Estate (R. 282), testified that they had a plan for development of their holdings in the vicinity (R. 287–290, 314–318), a portion of the lands here condemned being fifth or sixth in the order of development (R. 317–318). However, the schedule was revised because of the "tremendous amount of development work going on at Hickam Field and Pearl Harbor" so as to advance the time the condemned lands would be developed (R. 318). All of the witnesses believed that the lands could be successfully subdivided largely because of the demand created by Army and Navy personnel and defense workers (R. 177–178, 181–182, 205, 239–240, 285–291, 320, 326). The estimates of income upon which the capitalizations were based assumed that the subdivision would be accomplished five or six years in the future,

i. e., 1945 or 1946 (R. 218–219, 248–249, 346). The witnesses assumed not merely a continuance to 1946 of the defense housing demand but in fact based their valuations on the assumption that the demand "was going to accelerate very rapidly" (R. 345). Most of the witnesses further assumed that there would be no competition from other lands owned by the Damon Estate in the vicinity (R. 225–227, 253–254, 351–353). And Russell admitted that the rentals he capitalized could only be obtained by withholding those other lands from the market (R. 342).

The Government resisted admission of respondent's scheme of valuation by direct objections (R. 159, 161, 208), by motions to strike the testimony (R. 167–168, 194, 197, 219, 262, 314–315, 418–419), by requested charges (R. 90–91), and by motions for directed verdicts (R. 31, 71, 419). All of these objections were overruled. Some nine hours after the jury retired, the instructions concerning potential uses were repeated at the request of one of the jurors (R. 434–438). The verdicts were returned the next day (R. 440) and judgments were thereafter entered (R. 34–35, 75). The Circuit Court of Appeals affirmed [5] (R. 457–464).

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[5] The Government petitioned for rehearing, calling attention to the intervening decision of this Court in *United States* v. *Miller*, 317 U. S. 369. On February 6, 1943, an order was entered stating that the opinion had been written without consideration of the *Miller* decision and inviting a

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the value of agricultural land claimed to be adaptable for subdivision purposes may be determined by capitalizing the estimated income which might be produced if the lands were subdivided and leased for dwellings, business places, and truck gardens.

2. In holding that elements of value arising from a landowner's monopoly of undeveloped land may be included in the just compensation awarded upon condemnation of a small part of that land.

3. In holding that enhancement of value due to the project for which lands are taken may be included in the compensation paid for such lands.

4. In affirming the judgments of the district court.

SUMMARY OF ARGUMENT

I

All of respondents' witnesses based their valuations upon the estimated sales prices or the capitalization of estimated rentals which they thought could be obtained from residence, business, or truck farm lots after subdivision of the sugarcane lands. Such evidence was wholly incompetent and should have been excluded for the following reasons:

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supplemental memorandum on the applicability of that case (R. 468–469). Such memorandum was filed, but the petition for rehearing was subsequently denied (R. 464).

A. The conversion of farm land into a residential subdivision requires that many expensive improvements be made. For example, streets must be laid out and constructed, and water, sewage, electric lines, and other utility systems must be installed. When farm land is condemned, the probable use for residences may be considered "to the full extent that the prospect of demand for such use affects the market value." *Olson* v. *United States,* 292 U. S. 246, 255. But the land may not be valued as if the conversion to a successful residential subdivision had already taken place. Hence, valuations which are based upon the amounts for which the lots would sell or rent after subdivision are incompetent as evidence of market value of the farm land. *Chatfield* v. *Board of Revision of Taxes,* 346 Pa. 159, 29 Atl. 2d 685; *Pennsylvania S. V. R. Co.* v. *Cleary,* 125 Pa. 442, 17 Atl. 468; *Kansas City and Topeka Ry. Co.* v. *Splitlog,* 45 Kan. 68, 25 Pac. 202.

Moreover, respondents' valuations assumed that all of the lots in the projected subdivision could be sold five or six years in the future. Upon this hypothesis other assumptions were made as to the prices at which individual lots might be sold and the amount of the various expenses which would be incurred in subdividing the farm land. These speculations are likely to mislead a jury and introduce many collateral issues. For this additional reason, the evidence was not competent as

proof of the present market value of the farm land. *Laureldale Cemetery Co.* v. *Reading Co.*, 303 Pa. 315, 154 Atl. 372; *Burt* v. *Wigglesworth*, 117 Mass. 302; *Matter of City of New York (Blackwell's Island Bridge)*, 118 App. Div. 272, 103 N. Y. Supp. 441.

B. For similar reasons, valuations obtained by the capitalization of the estimated return from leases upon residence lots after subdivision of agricultural land are not competent evidence of the present market value of the farm land. The income is not attributable wholly to the land but represents the earnings upon the promoter's services and upon the investment in the improvements which would be required to develop the subdivision. Such valuations are highly speculative because they assume successful subdivision and leasing five or six years in the future. In addition, the allocation of income between land, improvements and promoter's services and the rate of interest at which the land income is to be capitalized have no factual basis but are entirely conjectural. *San Diego Land & Town Co.* v. *Neale*, 88 Cal. 50, 25 Pac. 977; *Pullman Co.* v. *Chicago*, 224 Ill. 248, 79 N. E. 572; *Hamilton* v. *Pittsburgh B. & L. E. R. Co.*, 190 Pa. 51, 42 Atl. 369; *New York Central R. R. Co.* v. *Maloney*, 234 N. Y. 208, 137 N. E. 305.

C. This is not a case where, among many other indicia of value, the capitalization of estimated

return from the assumed subdivision was considered and accorded the weight to which it might be entitled. This method of valuation was the principal basis of the opinions of respondents' experts. Where the experts' valuations are thus based on non-admissible items, their opinions of value are likewise inadmissible. *Atlantic Coast Line R. Co.* v. *United States,* 132 F. 2d 959, 963 (C. C. A. 5).

II

The notion that the lands condemned could be successfully subdivided and all the lots sold in five or six years was based on the assumption that a large area of contiguous lands, more than three times the acreage of the lands taken, would be withheld from competition. Elements of value arising from the fact that the owner may not want to part with the land because of its special adaptability to his own use must be disregarded in determining just compensation. *United States* v. *Miller,* 317 U. S. 369, 375. Since it is obvious that a willing buyer would not pay an increased value on the assumption that respondents would withhold their other lands from competition, there is no reason why the Government in a condemnation proceeding should be required to pay monopoly prices.

III

Commencing about May 1939, the military base at Pearl Harbor and Hickam Field was largely

expanded. At this time, authority was given and appropriation was made to acquire the specific lands here condemned in order to furnish housing required by the expansion project. The lands were condemned in November 1940. The housing demand created by "the tremendous development work going on at Hickam Field and Pearl Harbor" was the principal basis of the belief that the lands condemned could be successfully subdivided. It is therefore plain that the verdicts include enhancement of value occurring because of the project for which the lands were taken, contrary to the principle enunciated in *United States* v. *Miller*, 317 U. S. 369.

Respondents here went even further. The belief that subdivision could be successfully accomplished five or six years in the future was based upon the expectation that the Government's demand for housing "was going to accelerate very rapidly." Hence, the valuations included anticipated enhancement even after the taking.

ARGUMENT

I

THE PRESENT VALUE OF AGRICULTURAL LAND CLAIMED TO BE ADAPTABLE FOR SUBDIVISION PURPOSES MAY NOT BE ARRIVED AT BY CAPITALIZING THE NET INCOME WHICH, IN THE OPINION OF WITNESSES, COULD BE DERIVED FROM THE LANDS IF THEY WERE SUBDIVIDED AND LEASED FOR DWELLINGS, BUSINESS PLACES, AND TRUCK GARDENS

A. *Agricultural land may not be valued by hypothetically subdividing it into residence and business lots.*—In determining the market value

of property condemned, the highest and best use for which the property is adapted and needed or likely to be needed in the reasonably near future may be considered. *Olson* v. *United States*, 292 U. S. 246, 255. In this connection, the location of the property and other facts indicating existence of a demand for such purpose may be shown to the jury. But the courts have universally excluded evidence as to the number of lots into which agricultural land might be subdivided and the amounts at which the lots might sell or rent after subdivision. *Pennsylvania S. V. R. Co.* v. *Cleary*, 125 Pa. 442, 451, 17 Atl. 468; *Hall* v. *Delaware, L. & W. R. Co.*, 262 Pa. 292, 105 Atl. 98; *Laureldale Cemetery Co.* v. *Reading Co.*, 303 Pa. 315, 154 Atl. 372; *Chatfield* v. *Board of Revision of Taxes*, 346 Pa. 159, 29 Atl. 2d 685; *Kansas City and Topeka Ry. Co.* v. *Splitlog*, 45 Kan. 68, 72, 25 Pac. 202; *City of Los Angeles* v. *Hughes*, 202 Cal. 731, 262 Pac. 737; *Louisville & N. R. Co.* v. *R. E. E. De Montluzin Co.*, 166 La. 211, 116 So. 854; *Monongahela W. P. Pub. Serv. Co.* v. *Monongahela Develop. Co.*, 101 W. Va. 165, 132 S. E. 380; *Wadsworth Land Co.* v. *Piedmont Traction Co.*, 162 N. C. 314, 78 S. E. 299; cf. *Pullman Co.* v. *Chicago*, 224 Ill. 248, 79 N. E. 572; *Burt* v. *Wigglesworth*, 117 Mass. 302, 306; *Greenfield* v. *City of Philadelphia*, 282 Pa. 344, 354, 127 Atl. 768; *Matter of City of New York* (*Blackwell's Island Bridge*), 118 App. Div. 272, 274–275, 103 N. Y.

Supp. 441; *Tallman* v. *Met. El. R. R. Co.*, 121 N. Y. 119, 23 N. E. 1134; Schmutz, *Condemnation Appraiser's Handbook* (1938) p. 136. As the court said in *Pennsylvania S. V. R. Co.* v. *Cleary*, 125 Pa. 442, 452, 17 Atl. 468, 470:

> The jury are to value the tract of land, and that only. They are not to determine how it could best be divided into building lots, nor conjecture how fast they could be sold, nor at what price per lot. A speculator or investor in deciding what price he could afford to pay, would consider the chances and probabilities of the situation as then actually existing. A jury should do the same thing. They are not to inquire what a speculator might be able to realize out of a resale in the future, but what a present purchaser would be willing to pay for it in the condition it is now in. This is a rule that is well settled * * *.

The primary reason for the exclusion of evidence based upon the prospective sale price of individual lots after subdivision is that it assumes a state of facts which does not exist and consequently leads the jury astray. The rule permitting consideration of the best use for property does not mean that it is to be valued as if it were now used for such purpose. The prospective use is to be considered simply "to the full extent that *the prospect of demand* for such use affects the market value." *Olson* v. *United States*, 292 U. S. 246, 255; *United States* v. *Foster*, 131 F. 2d 3, 5–6

(C. C. A. 8), certiorari denied, 318 U. S. 767. Thus, in the present case, the jury was to value 331 acres of sugarcane land, considering its availability for subdivision purposes to the extent that the probable demand for such use affected the market value. There is a vast difference between a tract of agricultural land potentially valuable for a subdivision and the same tract of land after the real estate development has been successfully completed and the lots sold or rented. To convert farm land into residence property the land must be graded and filled. A portion of the land must be set aside for streets. Streets must be laid out and constructed, the consent of municipal authorities having been obtained. Sidewalks must be built. Water, sewage, electric lines and other utility systems must be constructed. And even more important than these physical improvements is the stimulation of demand which often requires the promoter, not only to advertise his subdivision widely, but, especially on large subdivisions, to provide retail stores and similar services (see R. 375).

Respondents' witnesses valued the land as if the promoter had successfully made these improvements. For example, they envisaged division of Lot D into two tiers of lots 60 feet by 150 feet with a street between, put a sales price or rental value on each lot and added them up to get the total (R. 197, 199–200, 210–211, 242, 261,

344–345). Such evidence "furnishes no proper measure of value, so far as the land appropriated is concerned, with which alone the jury has to do, and is well calculated to mislead the jury by furnishing a false and fanciful measure of damages." *Kansas City and Topeka Ry. Co.* v. *Splitlog*, 45 Kan. 68, 73, 25 Pac. 202, 204. Similarly, unimproved land may not be valued as if it were improved by a residence or industrial building, for "testimony as to what would be the fair rental value of the land with a suitable and proper building upon it related to mere matter of opinion as to the future, not of present fact, and was too prospective and indefinite in its nature to be competent evidence of the present value of the land, not built upon." *Burt* v. *Wigglesworth*, 117 Mass. 302, 306.

Such testimony should be rejected because it leads to speculation and collateral issues. Real estate developments are notoriously hazardous enterprises, and the cost of the unimproved land generally constitutes only one-third to one-fifth of the ultimate return if the promoter's hopes are realized (R. 258–259, 266–267, 373–374). Miscalculation of the demand is perhaps the most frequent cause of failure of such developments. Thus many promoters, like the respondents here, think that there is a certainty that a sufficient demand will exist when the project is completed but are disappointed because they have been too optimis-

tic or because intervening circumstances, such as changed economic conditions, have destroyed or diminished the demand. The speculation as to demand has particular importance here for the valuations contemplated sale or lease of lots five or six years in the future (R. 218–219, 248–249, 353). Russell, who represented all of the trustees (R. 340), assumed that the demand would permit disposal of the lots in 1945 or 1946 "without advertising, without effort, without paying any brokers" (R. 353). This sanguine view of the future was a prerequisite of respondents' valuations, because, as Castro admitted, at the date of taking in 1940 only "one-third of [the land] would be absorbed for homes" (R. 169).[4]

The valuations involved many other speculative elements such as the expense of physically improving the land by streets, sidewalks, utilities, etc. Thus, Castro testified (R. 170): "It would require special negotiation and systematic and intelligent financing in order to develop the area as a whole into a community section which in a

[4] For this reason, it is questionable whether any evidence as to alleged residence value of much of the property was admissible. Such evidence is permitted only if the property is "needed or likely to be needed in the reasonably near future." *Olson* v. *United States*, 292 U. S. 246, 255. Russell frankly recognized (R. 353) that "Some of those lots would be years off before they would be put on the market at all." Cf. *United States* v. *Foster*, 131 F. 2d 3 (C. C. A. 8), certiorari denied, 318 U. S. 767; *Hall* v. *Delaware, L. & W. R. Co.*, 202 Pa. 292, 105 Atl. 98.

reasonable period of time would be absorbed by the people in the market," and Russell spoke of the "hundreds of thousands of dollars" which would have to be spent for the development of roads, streets, and sewers (R. 352). Russell gave Lot D, which is nearest the navy yard, a lower relative value than another parcel because there would be greater expenses per acre of usable land (R. 327). In *Greenfield* v. *City of Philadelphia,* 282 Pa. 344, 354, 127 Atl. 768, 772, the court held that the value of office space per square foot in a building not yet erected was irrelevant to value of the land, stating: "There necessarily would be so many factors to be taken into account in determining what the net avails would be to the owner from the rents that the result of any determination reached from testimony as to what the rentals might be would be speculative in the extreme." And in *Matter of City of New York (Blackwell's Island Bridge),* 118 App. Div. 272, 274, 103 N. Y. Supp. 441, 443–444, the court reversed a determination of value because of the admission of testimony as to the rental value of apartments which might be erected on a vacant lot, stating: "This was clear error. It involved so much of the elements of uncertainty and speculation as to be inadmissible as proof of any fact."

The instant case involves conjecture to a much greater degree. Not only must assumptions be made as to the various expenses involved in subdividing

but the whole process hinges on a conclusion that conditions five or six years in the future will justify such expenditures. Such speculation will obviously lead the jury far afield from the question they are to determine, i. e., present value of the 330 acres of sugar-cane land. Cf. *Olson* v. *United States,* 292 U. S. 246, 257. The calculation employed by the experts have the semblance of mathematical certainty, whereas in truth they represent "at best, a guess by informed persons." *United States* v. *Miller,* 317 U. S. 369, 375. The jury, mislead by this appearance of mathematical exactness, gives too much weight to the resulting valuations. That the jury was misled in the instant case is evident from the fact that, having failed to reach a verdict in nine hours, a juror requested repetition of the instructions "with regard to the value of the properties within a restricted period" (R. 435). Like the landowner in *Tallman* v. *Met. El. R. R. Co.,* 121 N. Y. 119, 125, 23 N. E. 1134, 1135, who was permitted by the trial court to value vacant land as if it were improved, respondents have been permitted "to have all the advantages which [they] could derive from keeping [their land] substantially vacant and ready to sell as such, and at the same time to have all the advantages, without the investment of any money and without any risk, which [they] could have derived from their improved condition."

B. *Agricultural land may not be valued by capitalizing the estimated net income which might be earned after subdivision into lots.*—Valuations based upon estimated future profits from a business, present or prospective, on property condemned are almost uniformly rejected by the courts in eminent domain proceedings. *United States* v. *Meyer,* 113 F. 2d 387 (C. C. A. 7) (farm income), certiorari denied, 311 U. S. 706; *United States* v. *Davis,* 41 F. Supp. 595 (E. D. Tenn.) (farm income); *San Diego Land & Town Co.* v. *Neale,* 88 Cal. 50, 25 Pac. 977 (projected power project); *City of Stockton* v. *Vote,* 76 Cal. App. 369, 244 Pac. 609 (projected power project); *East Bay Municipal Utility Dist.* v. *Lodi,* 120 Cal. App. 740, 8 P. 2d 532 (projected power project); *Hamilton* v. *Pittsburgh B. & L. E. R. Co.,* 190 Pa. 51, 42 Atl. 369 (prospective bottling business); *Koesler* v. *Pittsburgh Ry. Co.,* 208 Pa. 50, 57 Atl. 66 (existing but not operating salt business); *Sparkill Realty Corp.* v. *State,* 268 N. Y. 192, 197 N. E. 192 (quarry); *Tacoma* v. *Nisqually Power Co.,* 57 Wash. 420, 107 Pac. 199 (projected power project); *Laureldale Cemetery Co.* v. *Reading Co.,* 303 Pa. 315, 323, 154 Atl. 372, 374 (future cemetery). But cf. *United States ex rel. T. V. A.* v. *Powelson,* 118 F. 2d 79 (C. C. A. 4), reversed on other grounds, 319 U. S. 266.

Valuations based on predicted rentals which might be realized after vacant property is improved are likewise rejected. *Burt* v. *Wiggles-*

worth, 117 Mass. 302 (fair rental value of vacant land if improved with suitable building); *Greenfield* v. *City of Philadephia*, 282 Pa. 344, 127 Atl. 768 (rental value of office space in building not yet erected); *Pullman Co.* v. *Chicago*, 224 Ill. 248, 79 N. E. 572 (rental of building not yet erected); *New York Central R. R. Co.* v. *Maloney*, 234 N. Y. 208, 137 N. E. 305 (estimated royalty under lease of non-existent brick business); *Matter of City of New York (Blackwell's Island Bridge)*, 188 App. Div. 272, 103 N. Y. Supp. 441 (rental of buildings, not yet erected); *Gage* v. *Judson*, 111 Fed. 350 (Conn.) (probable rental value or profits from office building not yet erected); cf. *Egan* v. *City of Philadelphia*, 108 Pa. Super. 271, 164 Atl. 813 (estimated rental for exhibition purposes). Such income is irrelevant in condemnation proceedings because it does not measure the value of the land and property actually taken. In most cases, only the land and the permanent improvements thereon are taken. The income derived from the business conducted on the property cannot be attributed solely to the real property. It is the result of all of the property and personal services used in producing the income and indicates the value of the business, not the property used in the business. See Orgel, *Valuation under Eminent Domain* (1936) secs. 154–157, 161, pp. 520–525, 529–536. As the court stated in *Matter of City of Rochester (Smith St. Bridge)*,

234 App. Div. 583, 587, 255 N. Y. Supp. 801, "It is the land which is appropriated, and not the business conducted thereon."

In the instant case the rentals which were capitalized represented the income on the subdivision development and not merely the land. The value of the land would constitute only a small part of the completed development which would be produced by construction of the various improvements. See *supra*, pp. 15, 16. The return from the completed subdivision would include income on the investment in the improvements and upon the personal services of the promoter. But the Government condemned simply the unimproved land. Hence the net income after deduction of current expenses such as taxes, water charges, etc. (see R. 194), cannot be wholly attributed to the land. The personal services furnished by the promoter are of particular importance because success or failure of a subdivision largely depends upon his skill. At least some of respondents' witnesses sought to avoid this objection by allocating the income between the land and the other factors which would produce the income. The details of this allocation do not appear, but Russell stated (R. 319):

> No, I reached that by a rather complicated figuring. We took the cost, and I might say it is a fairly well known cost from our past experience, of developing that land, putting in the developments re-

> quired. We have charged interest on that; we have charged depreciation on those costs, and the figure I have given you represents the capitalization of the net income after those have been deducted.

Thus, all of the net income was attributed to the land "after deducting service charges on the improvements" (R. 321). Such a method of allocating the income disregards the fact that the return is due just as much to the improvements and the promoter's services as it is to the land.[7] Cf. Schmutz, *Condemnation Appraiser's Handbook* (1938) pp. 11–12.

A second reason for exclusion of capitalization of estimated income or predicted rents is the highly speculative nature of such process. Respondents' predictions as to rentals involves the supposition that the subdivision will be successful so as to produce such rentals. Their witnesses assumed that general business conditions and the situation in the neighborhood of the property condemned would, five or six years in the future, permit leasing without any advertising or sales expense. Assumptions were also made as to the cost of improvements and the

[7] Successful subdivision usually produces an enhancement above the aggregate of the cost of land, cost of improvements and the cost of promoter's services. It is the hope for such enhancement which probably leads promoters to undertake such projects. Russell's method results in allocating all of the enhancement to the land alone.

amount of all other expenses involved in subdividing. Having made all of these assumptions, they capitalized at a rate of 4% to 5%.

The proper rate of interest to be used in capitalization is extremely important for a change from a 6% rate to a 5% or 4% rate will produce a 20% or 50% increase in value. To support their choice of a 4% to 5% rate, respondents introduced testimony that trust investments would return between 3% to 4% but the witnesses admitted that they were not qualified to advise on the rate of return on unimproved real estate which they considered to be speculative and therefore demanding a higher yield (R. 236–238, 306–309). So also the court excluded the Government's offer to prove that the Bishop Estate employed a 6% rate on its subdivision (R. 184–186). If a capitalization method were to be used, this collateral question as to the proper rate of interest would have to be fully investigated. And the untrained jury does not have the experience to pass upon such a question. Cf. Orgel, *Valuation under Eminent Domain* (1936) sec. 160, p. 529; Schmutz, *Condemnation Appraiser's Handbook* (1938) pp. 149–152.

Because of the many assumptions and collateral issues which would be introduced it is clear that a capitalization of predicted rentals from a hypothetical subdivision would be too untrustworthy to be of assistance in determining present market

value. The court said in *Greenfield* v. *City of Philadelphia*, 282 Pa. 344, 355, 127 Atl. 768, 772:

> Net rentals of an entire building might be of some assistance in determining its value from the income-producing standpoint, but to permit a witness to testify as to the market value of office space on the upper floors of a building on the lot in question, yet to be occupied by tenants, or to the market value of office space of other buildings in the vicinity, would get the jury out into the wildest realms of speculation on the question of the market value of the property.

All of the factors in respondents' process, which Russell characterized as "rather complicated figuring" (R. 319), were estimated. An apparently small change in any of these items would produce a great difference in the total valuation. Thus, Schmutz in discussing the application of a somewhat similar process to an existing building states (*Condemnation Appraiser's Handbook* (1938) p. 12):

> * * * the slightest change in the amount of the net income may make a great change in the value reflected. For example, a 10 per cent increase in the gross income may bring about a doubling in the net income to the land, with a consequent doubling in the capitalized land value. It is not uncommon to find a difference of 10 per cent in the net income which is wholly attributable to management.

In *Sharp* v. *United States,* 191 U. S. 341, this Court sustained the exclusion of offers to purchase or lease farm land for hotel, residential, or other purposes, stating (p. 348): "Pure speculation may have induced [the offer], a willingness to take chances that some new use of the land might in the end prove profitable."

In approving the exclusion of business profits as evidence of value, Orgel, *Valuation under Eminent Domain* (1936) states (sec. 173, p. 559):

> The courts have taken the proper course in avoiding this kind of valuation wherever possible because in the hands of unskilled jurors and judges on the one hand and of biased experts, on the other, there is no effective check on the value placed on properties by means of capitalization of earnings.

Neither *North American Telegraph Co.* v. *Northern Pac. Ry Co.*, 254 Fed. 417 (C. C. A. 8) nor *United States* v. *Shingle,* 91 F. 2d 85 (C. C. A. 9), the only authorities cited by the court below (R. 462), supports its conclusion. Those cases merely stand for the proposition that the capitalization of rentals accruing *from existing leases* is some evidence of value. In *McCandless* v. *United States,* 74 F. 2d 596 (C. C. A. 9), the court below held that opinions largely based on capitalization of rentals from existing leases on neighboring lands were inadmissable. The principal authority cited was *Pullman Co.* v. *Chicago,* 224 Ill. 248, 79 N. E. 572, where the court sus-

tained a verdict which completely disregarded valuation of vacant property based upon rentals the witnesses estimated would accrue from buildings erected thereon. This Court, in reversing on other grounds, stated (*McCandless* v. *United States*, 298 U. S. 342, 348):

> We find no reason to differ with the holding of the court below as to the inadmissibility of evidence respecting the rent paid for other lands.

Certainly, the evidence in the present case based upon the predicted rentals which might accrue after subdivision is much more speculative than the capitalization of existing rentals upon neighboring property excluded in the *McCandless* case.

C. *The fact that the experts stated that a willing buyer would use the method they employed does not render the evidence admissible.*—The court below admitted that valuation by capitalization of estimated rentals from an assumed subdivision involved "several variables" (R. 462). The only reason advanced to justify such a speculative process was the witnesses' assertions that a willing buyer would employ such a method. But plainly the mere fiat of experts does not prove the fact nor render speculations admissible. As Nichols states (2 Nichols, *Eminent Domain* (2d ed. 1917) sec. 445, p. 1171):

> The trial court cannot be too careful in excluding evidence of this character, as witnesses can always be found who will,

> in their imagination, cover the most hopelessly unmarketable vacant land in the neighborhood of a large city with apartment houses filled with desirable tenants. * * *

The ruling of the court below would deny judicial review of the testimony of any valuation expert no matter how incompetent or irrelevant it might be. For example, it is obvious that the courts will not permit evasion of the rule of *United States* v. *Miller*, 317 U. S. 369, by the expert's assertion that the willing buyer would consider enhancement arising from the project. All the authorities rejecting valuations based on predicted profits or estimated rents (*supra*, pp. 20–21) refute the reasoning of the court below, for the evidence is most frequently, if not invariably, offered by means of expert testimony.

This is not a case where the experts in reaching their opinion as to value used this process in conjunction with various other indicia of value. The fact that, in the course of his investigation, the expert became informed of various matters which would not be admissible in evidence such as tax assessments, offers, etc., does not necessarily lead to exclusion of his opinion. However, if the opinion is largely or completely based on inadmissible considerations, it is likewise inadmissible. *McCandless* v. *United States*, 74 F. 2d 596, 602–603 (C. C. A. 9), reversed on other grounds, 298 U. S. 342; *Atlantic Coast Line R. Co.* v. *United States*, 132 F. 2d 959, 963 (C. C. A. 5);

Orgel, *Valuation under Eminent Domain* (1936) secs. 131, 162, pp. 446–449, 536–539. Otherwise the rule excluding the evidence would be meaningless. Certainly, the fact that the method was employed by "experts"[8] in the instant case did not alter the speculative nature of the valuations.

Respondents' witnesses based their valuations solely on the capitalization of rentals or the estimated sales price of the lots after subdivision. The only mention of any other criterion of value is Castro's statement that his valuation was also based on fee simple prices (R. 179). However, he evaded an answer to questions designed to elicit what sales he was referring to (R. 180) and it is evident from his entire testimony that he used the same method as did respondents' other witnesses. Plainly, all of these opinions were admissible only on the assumption that the method of valuation the witnesses used was a proper measure of market value.

The result of admitting in evidence any valuation process which the expert states that a landowner would use would have important consequences at the present time when the Government is engaged in condemning some 8,000,000 acres of land for national defense and other purposes. The Government is repeatedly confronted with attempts of private landowners to inject into the

[8] Russell did not have any special knowledge as an expert. His testimony was admitted solely because he was one of the owners of the property (R. 313).

valuation proceedings grandiose plans for the development of unimproved property, the value to be determined by the capitalization of prospective profits or by the estimated prices of individual lots in a hypothetical subdivision.

II

ELEMENTS OF VALUE DUE TO A LANDOWNER'S MONOPOLY OF UNDEVELOPED LAND SHOULD BE DISREGARDED IN AWARDING JUST COMPENSATION FOR THE TAKING OF A PART THEREOF

In addition to the 331 acres of land here condemned the Damon Estate owns a large quantity of land in the neighborhood which is either undeveloped or is used for raising sugar cane. Thus the lease to the Honolulu Plantation Company embraced 1,451 acres (Defendant's Ex. 2 orig.; R. 312) and although the total acreage of the estate's land does not appear, it extended from two to two-and-a-half miles along Dillingham Boulevard (R. 174, 253, 317). All of this land was potential residence property to the same extent as was the land condemned (R. 174, 253). However, in concluding that the land condemned could be successfully subdivided, the witnesses assumed that the estate would withhold from competition all of the rest of this large area (R. 225–227, 253–254, 351–353).

This assumption was an essential part of the values claimed by respondents. Their witnesses refused to state to what extent competition would

reduce their estimates (R. 254–255, 351–353). Obviously, the release of more than 1,100 acres to competition would substantially diminish if not completely remove the possibility of successfully subdividing the 331 acres.[9] As Kearns expressed it (R. 254), "we had in mind that it had a greater value to the present owners than to anyone else." In *United States* v. *Miller,* 317 U. S. 369, this Court reemphasized the rule that such values may not be included in just compensation, stating (p. 375):

> Again, strict adherence to the criterion of market value may involve inclusion of elements which, though they affect such value, must in fairness be eliminated in a condemnation case, as where the formula is attempted to be applied as between *an owner who may not want to part with his land because of its special adaptability to his own use,* and a taker who needs the land because of its peculiar fitness for the taker's purposes. *These elements must be disregarded by the fact finding body in arriving at "fair" market value.* [Italics supplied.]

It is clear that a willing buyer would not pay an increased value for the 331 acres on the as-

[9] Russell's subdivision contemplated a larger number of lots than there were houses constructed in all of Honolulu in either 1940, 1939, 1938, or 1937. In those years between 1,000 and 1,600 dwelling units were built (R. 372–373; see also R. 175–176) while Russell divided the land into some 1,531 lots (R. 345, 353).

sumption and without assurance that respondents would withhold their other lands from competition. No reason appears why the Government should be required to pay such monoply prices, especially when there is nothing to prevent respondents from immediately subdividing their other lands.

Apparently the court below thought that the charge to the jury cured this error (see R. 461). But this element was essential to respondents' valuation process. The witnesses refused to estimate to what extent competition would reduce their estimates. Hence, the jury had no basis from which to determine whether any subdivision would have been possible if competition existed or, if so, to determine the amount by which the valuations should be discounted. Thus, it is quite possible that, excluding the monopoly, the respondents' valuations would not have been very much higher than those of the Government. The witnesses' opinions lacked probative value and should have been excluded. Under these circumstances, the instructions to the jury could cure the error only by plainly telling the jury to disregard the opinions or, at least, that elements of value attributable to the estate's monopoly must be disregarded. No such instruction was given. Rather than plainly excluding monopoly value, the instruction permitted the jury to include this

element in its verdict."[10] Cf. *Maytag* v. *Cummins*, 260 Fed. 74, 82–83 (C. C. A. 8); *Harkins* v. *Brown*, 108 Fed. 576 (C. C. A. 4). And the fact that the verdicts closely approached the estimates of Harrison and Kearns (within 20%) persuasively indicates that the jury did include this element in the awards (see R. 461).

III

THE JUDGMENTS INCLUDE ENHANCEMENT OF VALUE RESULTING FROM THE PROJECT FOR WHICH THE LANDS WERE TAKEN

The expansion of the naval and military base at Pearl Harbor and Hickam Field was one of the most important projects in connection with the national defense program. An integral part thereof was the securing of housing for military and civilian personnel. Other negotiations having failed, authority was granted to condemn a site for such purpose and an appropriation to pay for the site was included in the Act of May 25, 1939, 53 Stat. 757, 774. The hearings upon this Act make it plain that the appropriation was made in order to acquire the specific lands condemned in this case (see Appendix *infra*, pp. 37–39)

[10] The charge stated (R. 428) "you are not bound to assume that the Trustees of the Damon Estate would not release any of the lands in the immediate vicinity from their present status."

Moreover, it is equally plain that respondents' witnesses based their estimates largely upon the greatly increased demand resulting from the expansion program undertaken in 1939 (R. 205, 239–240, 285–291, 315, 320, 326). The trustees of the Damon estate had a long-range plan for development of the large area they owned on which the lands condemned came fifth or sixth."[11] However, the lands condemned were advanced on the list because of "the tremendous amount of development work going on at Hickam and Pearl Harbor" (R. 318). Thus, there can be no doubt that the verdicts include enhancement of value because of the expansion of the military base occurring after the specific appropriation was made and the condemnation of these lands was authorized.

Moreover, all of respondents' valuations assumed that the sale or leasing would occur, not at the date of taking in 1940, but five or six years in the future (R. 218–219, 248–249, 346). And they assumed, not merely a continuance to 1946 of the demand caused by the tremendous national defense development, but rather they thought "the land is certain to increase in value

[11] The first four subdivisions under this plan were developed in 1924, 1929, 1933, and 1938 (R. 271–272, 283–286). All of these developments over the 16-year period, totaling 321 acres (R. 271, 284–286), were located in the direction of Honolulu rather than towards Pearl Harbor (R. 342–343; see Government's Ex. C. orig.).

there" (R. 319; see also R. 263–264, 270). In fact, Russell testified as follows (R. 345–346):

> Q. Did you assume that the market as of November, 1940 was going to continue?
>
> A. We thought it was going to accelerate very rapidly.

The method of valuation employed here has thus resulted in compelling the Government not only to pay enhancement occurring between the date the Government was committed to the project and the date of taking but also enhancement which respondents expected the Government's demand for housing would cause in the future. This case, therefore, falls squarely within the rule of *United States* v. *Miller*, 317 U. S. 369. Cf. *United States* v. *Rayno*, 136 F. 2d 376 (C. C. A. 1), certiorari denied October 25, 1943 No. 351, this Term.

Both the trial of this case and the hearing in the circuit court of appeals having occurred prior to this Court's decision of the *Miller* case, this question was not presented in the courts below until the petition for rehearing was filed. In response to the order of the court below of February 6, 1943 (R. 468–469), a memorandum was submitted setting forth the facts which demonstrate the applicability of the *Miller* decision. However, the petition for rehearing was denied (R. 464). *In Vandenbark* v. *Owens-Illinois Co.*, 311 U. S. 538, this Court reversed a judgment for

failure of the circuit court of appeals, in applying the rule of *Erie Railroad Co.* v. *Tompkins*, 304 U. S. 64, to consider a reversal of the local law which occurred after the trial court's judgment was entered. Compare *Hormel* v. *Helvering*, 312 U. S. 552, 557. The judgments in the instant case charge the Government with elements of value which the public should not, in fairness, be required to pay. In the circumstances of this case, the failure of the Government to raise the issue specifically at the trial should not require payment of enhancement occurring after May 25, 1939.

CONCLUSION

It is respectfully submitted that the judgment of the circuit court of appeals should be reversed.

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APPENDIX

Comparison of testimony of Rear Admiral Ben Morreel, Chief of Bureau of Yards and Docks on April 5, 1939 before House Subcommittee on Appropriations (page 416 of Hearings) with facts in the record.

Testimony	*Facts in Record*
NAVY YARD, PEARL HARBOR, HAWAII	
PURCHASE OF LAND	
Mr. FERNANDEZ. The first item is $165,000 for the purchase of land at the Navy Yard, Pearl Harbor, Hawaii.	
Admiral MORRELL. This project was authorized by the act of June 25, 1938.	
The Pearl Harbor Navy Yard is the principal outlying naval base of the United States and is a most important activitiy for the repair, upkeep, and support of the United States Fleet in the Pacific. The area of the naval base is limited and there is not sufficient land for the development of housing areas for industrial civilian personnel and enlisted personnel.	
The housing situation in the vicinity of Pearl Harbor is acute and efforts have been made through the Federal Housing Administration to secure low-priced housing for officers, enlisted, and civilian personnel. To date	Russell testified he knew the Navy was interested in having the Damon Estate erect a series of low costs to relieve the housing shortage at Pearl Harbor (R. 337).

Testimony	*Facts in Record*
no satisfactory solution has been reached and it appears impracticable to obtain the needed housing by reliance on private parties.	
This project contemplates the acquisition of a tract of land adjacent to the navy yard, to be developed as funds become available, for housing of the various classes of personnel attached or assigned to the station. It is proposed that this area be developed to meet the immediate needs to relieve the present acute housing situation, with provision for future expansion in time of emergency.	Russell testified the urgent demand for the lot just outside the navy yard gate had been present for a year and a half before November 1940, i. e., about June 1939 (R. 318). He also stated that Army and Navy activities particularly affected the demand for this lot (R. 320).
The area contains about 350 acres.	The lands condemned total 331.756 acres (R. 22, 42).
Mr. FERNANDEZ. Did that authorization contemplate the utilization of this land for civilian employees?	
Admiral MOREELL. Yes, sir.	
Mr. FERNANDEZ. Has there been an expansion of the civilian personnel there recently?	
Admiral MOREELL. Not in the immediate past; no, sir.	
Mr. FERNANDEZ. Is there any other land in this immediate vicinity that is suitable for quarters?	The land adjoins Pearl Harbor and Hickam Field. See map, Ex. G, original.
Admiral MOREELL. No, sir.	
Mr. FERNANDEZ. How do you arrive at the figure of $165,000?	The deposit for land and improvements of $157,369.94 (R. 22, 57) equals about $474 per acre. $165,000 for 350 acres equals about $471 per acre.
Admiral MOREELL. That is a figure estimated by the Commandant. The land belongs to several estates, and I understand that by the	

Testimony	*Facts in Record*
terms of the trusteeship they are not allowed to quote a price. I have here a statement from the Commandant, from which I quote as follows: It was evident, from negotiations with owners of these parcels, that they were very reluctant to fix definite prices for the parcels in question. The Commandant is of the opinion, however, that the amount of $165,000 is sufficient to cover all of the tracts proposed to be purchased. An area of 244 acres is classed as cane land, 48 acres are classed as pasture land, 72 acres as fishponds and waste lands, and approximately 1½ acres are classed as semi-commercial lands. The average price per acre approximates the price awarded in condemnation proceedings for land of high potential value for agriculture. That would approximate the price paid by the Army for Hickam Field, or $441 per acre.	Russell, one of the trustees of the Damon Estate certified that in 1939 and 1940 negotiations were had with the Navy Department relating to a housing development (R. 326, 335–337).

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